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Supreme Court of the United States

OCTOBER TERM, 1948

No. 168

THE CITY OF NEW YORK,

Petitioner,

against

LEWIS H. SAPER, Trustee in Bankruptcy of SPOTLIGHT PRODUCTIONS, INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER

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Supreme Court of the United States

OCTOBER TERM, 1948

No. 168

THE CITY OF NEW YORK,

Petitioner,

v.

LEWIS H. SAPER, AS TRUSTEE IN BANKRUPTCY OF SPOTLIGHT PRODUCTIONS, INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER

A writ of certiorari was granted by this Court on October 11, 1948 (R. 40), to review an order (R. 38) of the United States Circuit Court of Appeals for the Second Circuit, affirming in part and reversing in part an order in bankruptcy (R. 28-29) made by the United States District Court for the Southern District of New York (COXE, J.), which allowed the claim of the petitioner against the trustee in bankruptcy for sales taxes and business taxes due the petitioner in the respective sums of $495.61 and $19.72, and allowed interest on such claims until the date of payment. The Circuit Court of Appeals' order affirmed the allowance of the petitioner's claim in the sums speci-

fied but provided that interest should run only until January 5, 1944, the date of the filing of the petition in bankruptcy.

The sole issue presented is whether interest on the petitioner's claim for taxes due from the bankrupt is to be allowed to the date of payment or only until the date of the filing of the petition in bankruptcy.

Opinions Below

The opinion of the District Court is reported in 75 Fed. Supp. 458.

The opinion of the Circuit Court of Appeals is reported in 168 Fed. (2nd) 268.

Grounds of Jurisdiction

The jurisdiction of this Court is invoked under Judicial Code, §240, 28 U.S.C.A. §347, subd. a. The order of the Circuit Court of Appeals was entered May 27, 1948. The petition for a writ of certiorari was filed on July 21, 1948 and was granted on October 11, 1948.

Statement of the Case

(1)

The petition in bankruptcy was filed January 5, 1944 (R. 32). On May 17, 1944 the petitioner, the City of New York, filed a proof of claim for $750 for sales taxes for the period from October 21, 1934 to January 5, 1944, and for $250 for business taxes from 1933 to 1943 (R. 2). The trustee objected and moved before the Referee for

an order expunging the claim (R. 5). On July 18, 1947 the City filed an amended proof of claim for sales taxes and business taxes for the period from November 1, 1940 to May 30, 1942 in the sums of $495.61 and $19.72, respectively, as principal, and $341.97 and $13.13, respectively, as interest at the statutory rate of 1% per month (R. 3-5).

Hearings were held before the Referee at which it appeared that no sales tax returns or business tax returns for the period November 1, 1940 to May 30, 1942 had been filed by the bankrupt (R. 18). Joseph Schlissel, an accountant employed by the petitioner, examined the records of the bankrupt and gathered together the figures upon which the petitioner's amended claim was based (R. 11). He testified (R. 12-16) and the Referee found (R. 19-20) that on the basis of sales made during the period involved $495.61 was due for sales taxes and $19.72 for business taxes. The Referee allowed those two amounts together with interest at the statutory rate of 1% per month until paid (R. 20, 23).

(2)

Upon review, the District Court (COXE, J.) affirmed the order of the Referee. In his opinion (R. 26-27) the District Judge stated that the petitioner was entitled to interest on its claim to the date of payment, citing *In Re J. Menist & Co.*, 290 Fed. 947 (C.C.A. 2, 1923), modified on other grounds *sub. nom. United States v. Childs*, 266 U. S. 304 (1924). The Court held that the rule had not been changed by the 1938 amendments to the Bankruptcy Act and cited *Davies v. Green*, 133 Fed. (2nd) 451 (C.C.A. 1, 1943).

The Circuit Court of Appeals reversed the order of the District Court in so far as it allowed interest on the City's claim to the date of payment. The opinion by Judge CLARK (R. 31-38) held that the 1938 amendments to the Bankruptcy Act had brought tax claims within the provisions of §63a and thereby placed them on a parity with ordinary claims so far as interest was concerned, and that interest did not accrue on any claims during the period of bankruptcy administration. Accordingly, the Court allowed interest on the City's claim only until January 5, 1944, the date of the filing of the petition in bankruptcy.

Specification of Errors to be Urged

We contend that the Circuit Court of Appeals erred in allowing interest on the City's claim only until the date of the filing of the petition in bankruptcy. Such interest should have been allowed to the date of payment.

Summary of Argument

Prior to the enactment of the Chandler Act in 1938 (52 Stat. 840), the decisions of this Court had settled the law to the effect that interest on a tax claim in bankruptcy runs until the date of payment of the claim. We shall analyze in our argument all of the changes as to tax claims made by the Chandler Act, and shall urge that they fail to show any intent to change the law that interest on tax claims runs until the date of payment but, on the contrary, indicate that Congress intended to leave that law unchanged.

The Chandler Act reenacted with only a minor change not here relevant §57j of the Bankruptcy Act providing for the payment of interest on tax claims. It thereby evidenced an intent that the rule as to the running of interest on tax claims to the date of payment should remain unchanged.

The Chandler Act also; (1) amended §57n of the Bankruptcy Act so as to require that tax claims be filed; (2) eliminated the provision in old §64a requiring the Court to order that tax claims be paid since that provision was no longer necessary because tax claims had to be filed under the amendment to §57n; (3) reenacted §64a leaving substantially unchanged the order of priority payments with respect to tax claims; and (4) reenacted §17 providing that tax claims are not dischargeable in bankruptcy if unpaid.

The change in §57n was designed to facilitate the administration of bankrupt estates and eliminate the necessity of the trustee obtaining bar orders as to tax claims. The change in §64a was an incident of the change in §57n. Those changes were of an administrative character and do not indicate an intent to change the rule that interest on tax claims runs until the date of payment. This is particularly true when the changes in §57n and old §64a are coupled with the provisions of the Chandler Act leaving substantially unchanged the order of priority payments with respect to tax claims (new §64a), and reenacting without material change §§57j and 17.

ARGUMENT

Tax claims in bankruptcy bear interest to the date of payment. The Chandler Act, so far as it related to tax claims, facilitated the administration of bankrupt estates by requiring tax claims to be filed and made certain other minor changes, but did not change the established rule that interest on taxes runs to the date of payment.

(1)

Prior to the passage of the Chandler Act (52 Stat. 840) in 1938, the rule was well established that by virtue of the provisions of §57j tax claims in bankruptcy bore interest to the date of payment:

Meilink, Trustee v. *Unemployment Reserves Commission of California,* 314 U. S. 564 (1941);
United States v. *Childs,* 266 U. S. 304 (1924); modifying *In re J. Menist & Co.,* 290 Fed. 947 (C.C.A. 2, 1923);
People of the State of New York v. *Jersawit,* 263 U. S. 493 (1924);
Dayton v. *Pueblo County,* 241 U. S. 588 (1916);
Horn v. *Boone County,* 44 Fed. (2nd) 920 (C.C.A. 8, 1930);
In re Kallak, 147 Fed. 276 (D. C. N. Dakota, 1906).

In *In re J. Menist & Co., supra,* the Circuit Court of Appeals, Second Circuit, affirmed an order of the District Court in a bankruptcy proceeding directing the payment

of a tax to the United States with interest at the rate of 6% per annum to the date of payment. The Court rejected the Government's claim to interest at the rate of 1% per month on the ground that that rate was a penalty, the payment of which was forbidden by §57j of the Bankruptcy Act. In its opinion the Court said, per HOUGH, J. (290 Fed. at pp. 949-950):

> "The question remains whether a tax demand, duly proved, should continue to draw interest at the legal rate after the filing of petition for adjudication. The general rule is, of course, that interest stops with petition filed (Sexton *v.* Drefus, 219 U. S. 339, 31 Sup. Ct. 256, 55 L. Ed. 244), but a tax debt, due to any of the taxing authorities enumerated in section 64a, is not only a highly preferred debt, but the section contains specific directions that the trustee shall pay 'all taxes legally due and owing.' That means legally due and owing in accordance with the provisions of the Bankruptcy Act, and under that statute section 57j requires penalties due to the United States, or a state, etc., to be allowed to the extent of the pecuniary loss suffered. The loss continues as much after petition filed as before.
>
> We agree with the court below that these directions cannot be fulfilled, except by an order on the trustee to pay the tax, with lawful interest down to the date of actual payment."

This Court reversed the Circuit Court with respect to the rate of interest and held that it should run at the rate of 1% per month, but affirmed so much of the decision of the Circuit Court as held that interest should run on the claim until paid, *United States* v. *Childs, supra.* Upon the appeal to this Court the respondent specifically urged

that interest should not run after the filing of the petition (see 266 U. S. at p. 30). The ruling of this Court settled the law to the effect that interest on tax claims runs until the date of payment.

Meilink, Trustee v. *Unemployment Reserves Commission of California, supra,* reached this Court in 1941, considerably subsequent to the passage of the Chandler Act. This Court cited *United States* v. *Childs, supra,* and affirmed an order of the Circuit Court of Appeals, Ninth Circuit, in a bankruptcy proceeding holding that a State tax should bear interest at the rate of 1% per month to the date of payment and that that rate did not constitute a penalty within the meaning of §57j of he Bankruptcy Act. The question as to the effect of the Chandler Act upon the rule laid down in *United States* v. *Childs, supra,* does not appear to have been argued.

Administrative Code of the City of New York, §N41-17.0, subd. a, and §§R41-14.0, subd. a, and RR41-14.0, subd. a, *infra,* pp. 21-22, providing for interest on unpaid taxes at the rate of 1% per month, are similar to the statutes involved in the *Childs* and *Meilink* cases. In any event, no contention is made by the trustee herein that interest is not allowable at the statutory rate. Applying the *Childs* and *Meilink* decisions to the instant case, it is clear that at least prior to the passage of the Chandler Act, interest on the petitioner's tax claim here involved would run to the date of payment at the rate of 1% per month.

(2)

The contention that the rule as to the running of interest on tax claims was altered by the Chandler Act requires a detailed examination of the changes effected

by that statute with respect to tax claims. We have set forth verbatim in the appendix hereto, *infra*, pp. 24-33, the relevant provisions of the Bankruptcy Act before and after the 1938 amendments and shall now analyze them.

(a)

Section 57j of the Bankruptcy Act (11 U.S.C.A. §93, subd. j) was reenacted by the Chandler Act with only a minor change, the substitution of the phrase "any State or subdivision thereof" for the phrase "a State, a county, a district, or municipality".

As reenacted by the Chandler Act §57j reads as follows:

> "Debts owing to the United States or any State or subdivision thereof as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law."

We submit that the reenactment of this section, practically unchanged, by the Chandler Act is of the greatest significance in considering the problem posed by the instant case. It was indeed the principal ground upon which the Court in *Davie v. Green*, 133 Fed. (2nd) 451 (C.C.A. 1, 1943), reached a conclusion contrary to that of the Circuit Court herein, and it was also relied on by Judge Augustus N. Hand in his opinion in *Carter v. United States*, 168 Fed. (2nd) 272 (C.C.A. 2, 1948), which favors our position herein.

In *Davis v. Green, supra*, the Court said per Woodbury, J. [133 Fed. (2nd) at p. 453]:

> "In 1938 when Congress passed the Chandler Act it made many fundamental and far-reaching changes in the law of bankruptcy, but it made only a minor verbal change in §57, sub. j of the Bankruptcy Act of 1898.[1] It left untouched the last words of that section which provide for the payment of debts due the United States or any State or subdivision thereof with 'such interest as may have accrued thereon according to law' which words the courts had repeatedly construed, rightly or wrongly, to mean interest to the date of payment. It is fair to assume that Congress in thoroughly revising the law of bankruptcy became aware of the construction which the courts had placed upon the words which it had previously used, and that if it had wished to change that construction so as to place claims for taxes on the same footing with other claims with respect to interest it would have said so in clear and unmistakable terms. If the old interpretation, to which we feel obliged to adhere, works injustice or hardship upon the general creditors of a bankrupt, relief for them must be sought in Congress."

To this comment we add the fact that on June 8, 1948, the House of Representatives passed a bill introduced by Congressman Reed (H.R. 5693, 80th Congress, 2d Session) to amend the Bankruptcy Act in several respects. Section 11 of the bill provided for the amendment of §57j of the Bankruptcy Act to read as follows:

> "Sec. 57j. (*1*) Debts owing to the United States or *to* any State or any subdivision thereof as a penalty or forfeiture shall not be allowed, except

---

"1. It only substituted the phrase 'any State or subdivision thereof' for the phrase 'a State, a county, a district, or a municipality.' (Footnote is part of the opinion.)

for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued [thereon according to law] *on the amount of such loss up to the date of bankruptcy.*

(2) Except where the estate of the bankrupt is solvent, interest accruing after the date of bankruptcy on taxes legally due and owing to the United States or to any State or any subdivision thereof shall not be allowed."[1]

The bill was referred to the Senate Committee on the Judiciary on June 9, 1948 but no action was taken on it prior to the adjournment of Congress or at the recent special session.

The fact that this bill was introduced strongly indicates that the Chandler Act was not intended to change the rule that interest on tax claims runs to the date of payment and the report of the House Committee on the Judiciary with respect to the bill expressly so states.[2]

The Circuit Court, in its opinion herein (R. 37), stated in substance that §57j was not determinative of the question involved because "it seems clearly to be operable only *after* the question as to what, if any, interest is legal has been decided" (Italics the Court's). With due deference, we submit that this comment fails to give full meaning to the wording of the section. Section 57j was and is a clear mandate to pay interest on taxes "according to law", and the settled law prior to the Chandler Act was that such interest ran to the date of payment. If Congress meant to

1. Italicized words are new and bracketed words are to be eliminated.

2. House of Representatives, 80th Congress, 2d Session, Report No. 2083, dated May 28, 1948. The report contains a "General

change that law, the obvious way to do it was to amend §57j accordingly. The Chandler Act, however, made no material change in §57j and by reenacting it evidenced an intent to leave the rule as to interest on taxes unchanged.

Statement" as to the passage of the Chandler Act of June 22, 1938 and refers to the desirability of making certain changes therein. With respect to the proposed changes in §57j the report states:

"'11. Section 11 (a) of the bill is intended both to clarify and modify section 57j of the act. The change in 57j (c) is to make clear that the limitation on interest up to the date of bankruptcy relates only to interest on the 'pecuniary loss,' and further that such interest stops at the date of bankruptcy. The addition of clause (2) in the bill is intended to overrule an obsolete rule as to interest on delinquent tax debts. Interest on general unsecured debts, on unsecured Government debts other than taxes, and on debts entitled to priority under section 64-a, is suspended at the date of bankruptcy so that, except in the rare case of a solvent estate, interest is allowable only to such date. (Sec. 63a; *Adams v. Napa Cantina Wineries* (C.C.A., 9th Cir.), 36 Am. B. R. (N.S.) 8 [94 Fed. (2nd) 694 (1938)]; *In re Gandelfi & Co., Inc.* (S.D. N.Y.), 51 Am. B. R. (N.S.) 521 (governmental debts and other debts entitled to priority); 3 *Collier on Bankruptcy*, 14th Ed., 1835 *et seq.*; 2 *Remington on Bankruptcy*, 4th Ed., secs. 771, 795.) However, interest on delinquent tax debts is allowable to the date of payment (*In re Kallak* (D.C.N.D., 1906); 17 Am. B.R. 414; *In re Ashland Emery and Corundum Co.* (D.C. Mass., 1916), 36 Am. B.R. 194 [229 Fed. 829]; *In re Clark Realty Co.* (C.C.A., 7th Cir., 1918), 42 Am. B.R. 403 [253 Fed. 938]; *sub silentio: United States v. Childs*, 266 U. S. 304, 307 (1924), 5 Am. B.R. (N.S.) 5). *Although, under the Chandler Act, a tax debt is required to be proved (sec. 57n) and its order of priority ranks below all administration costs and expenses, wages and costs and expenses of creditors successfully opposing a settlement or discharge, or procuring a conviction for an offense (sec. 64a (1), (2), (3)), thereby rendering obsolete the reasoning in the Kallak case, nevertheless its rule has not been changed, and therefore requires this statutory modification.* For further discussion see *In re D. O. Summers* (Ref. N.D. Ohio, 1939), 46 Am. B.R. (N.S.) 123; *In re Dorsey* (Ref. W.D. Wash., 1940), 46 Am. B.R. (N.S.) 146; *Davis v. Green* (C.C.A. 1st Cir., 1943), 52 Am. B.R. (N.S.) 603. And on overruling the *Kallak* case see *In re Union Fabrics, Inc.* (S.D. N. Y., 1947), 73 F. Supp. 685, appeal pending." (Italics supplied.)

(b)

The principal change effected by the Chandler Act with respect to tax claims was the amendment of §57n (11 U.S.C.A. §93, subd. n) so as to provide that tax claims be filed within six months after the first date set for the first meeting of creditors, with provision for the Court granting a reasonable extension of time. It is clear that this change was designed to facilitate the administration of bankrupt estates by obviating the necessity of the trustee obtaining bar orders against taxing authorities.

Prior to the Chandler Act, there was no requirement in the Bankruptcy Act that tax claims be filed. Section 57n, which provided for the filing of claims generally, was silent as to tax claims and was therefore held to be inapplicable to them. The result was that the practice had grown up of the trustee asking the Court to issue an order requiring tax claims to be filed within a certain date or be barred. This practice was the only safe and practicable means of administering a bankrupt estate and its validity was upheld by the Courts on numerous occasions. *New York* v. *Irving Trust Co.*, 288 U. S. 329 (1933). Failure to obtain a bar order had the effect of leaving the trustee personally liable for unpaid taxes. *Cf. United States* v. *Kaplan*, 74 Fed. (2nd) 664 (C.C.A. 2, 1935). But even when a bar order was obtained, the Court was empowered to revoke it upon a showing of circumstances justifying such action: *New York* v. *Irving Trust Co.*, *supra*; *United States* v. *Elliott*, 57 Fed. (2nd) 843 (C.C.A. 6, 1932).

This led to uncertainty in the administration of bankruptcy estates which the changes made in §57n by the Chandler Act were designed to overcome. The House

Report[1] and Senate Report[2] on the Chandler Act both make this abundantly clear.

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1. The House of Representatives, 75th Congress, 1st Session, Report No. 1409, dated July 29, 1937, to accompany H.R. 8046, states as follows (p. 3):

> "The bill seeks to accomplish the following general purposes [ten purposes are mentioned of which number 2 is here pertinent]: * * *
>
> "(2) **To increase efficiency in administration.**"

And in discussing this purpose, under the caption **"Amendments to increase efficiency in administration"** (p. 8), the Report states (p. 13):

> "(3) *Claims-Filing*—Section 57: Subdivision n relating to the filing of claims has been entirely recast, and several significant changes have been made.
>
> All proofs of claim, except as otherwise provided in chapters X, XI, XII and XIII, including claims for taxes and debts owing to a government, must be filed and proved. *The provision in respect to government claims is added in order to overcome the decisions which hold that the bar time for the filing of claims is not binding upon a sovereign.* Thus the administration of the estate is speeded up, and the distribution becomes more certain and definite." (Italics supplied.)

2. The Senate, 75th Congress, 3rd Session, Report No. 1916, dated April 20, 1938, to accompany H.R. 8046 states as follows (p. 2):

> "The provisions dealing with claims of Federal and State Governments, particularly with respect to the proving and filing of such claims and the dischargeability of tax claims require modernization."

And speaking of §57n (p. 5):

> "5. *Including government claims within bar time—Extension of time*—**(Sec. 57, subdivision n, p. 76, lines 7 and 10-13).**—The House Bill includes within the bar time for the proving of claims, all claims of the United States and of any State or subdivision thereof. The committee has both strengthened and extended this proposed amendment by providing, first, that such claims must actually be filed within the bar time, and, second, by permitting additional time for the filing of such claims upon application for cause shown. The committee agrees with the proposal that governmental claims should be subjected to the same requirements as other claims but is of the opinion that the limitation should be tempered by the provision for extension, for the reason that it is sometimes difficult for the Government to prepare and present its claims within a fixed time. The limitation will speed up the closing of estates, and the extension will provide a reasonable flexibility."

(c)

In its opinion herein (R. 34-35), the Circuit Court placed an entirely unwarranted emphasis upon the elimination of old §64a by the Chandler Act. The only provision of old §64a which was eliminated was that which required the Court to order the trustee to pay taxes owing by the bankrupt. Even without such a provision the Court was required to direct payment of taxes and the trustee had the obligation to search them out and pay them. *Lewis, Trustee* v. *United States*, 92 U. S. 618 (1875). However, even if that provision had been necessary in order to effect proof and payment of tax claims, the Chandler Act amendment of §57n so as to require the proving and filing of tax claims rendered that portion of old §64a obsolete and unnecessary. Hence the elimination of that provision of old §64a by the Chandler Act is without significance on the issue here.*

* The House Report on Public Bills, 75th Congress, 1st Session, Report No. 1409, dated July 29, 1937, to accompany H.R. 8046 discussed the changes in §§64a and 64b as item (4) under "**Amendments to increase efficiency in administration**" (p. 8) immediately after the discussion of the changes in §57n, which is item (3) (see footnote 1, p. 14, *supra*). Concerning the changes in §64, the Report states (p. 15):

> "(4) *Priorities*—Section 64: Subdivisions a and b have been merged and recast. Subdivision (a) in the present act, which relates to the payment of taxes, has been eliminated, and the subject of taxes transferred to the fourth order of priority in our merged subdivision, which now of course becomes subdivision (a). The limitation in amount of real estate taxes, and the conferring upon the court of jurisdiction to determine the amount or legality of all taxes, are retained. The present subdivision b, which is our new subdivision (a), has been considerably modified. Clauses (1), (2) and (3), which previously classified the costs and expenses of the proceedings in the order prescribed, have been combined and all such costs and expenses given a single order of priority."

The portions of old §64a limiting claims for tax assessments against real property to the value of the bankrupt's interest therein, were broadened to apply to assessments against all property and were incorporated in new §64a. The provisions of old §64b were also incorporated into new §64a by the Chandler Act, without any material change with respect to the priority status of tax claims.

(d)

The Circuit Court also seems to have labored under the impression that the Chandler Act amendments to §§57n and 64a brought tax claims within the provisions of §63a of the Bankruptcy Act (11 U.S.C.A. §103, subd. a), which relates to provable claims and provides that interest on such claims be allowed to the date of the filing of the petition in bankruptcy. Judge CLARK's opinion expressly so states (R. 35). We submit that in this respect the Court was clearly in error. Both before and after the Chandler Act tax claims are nowhere mentioned in §63a and are therefore necessarily excluded therefrom. *Guarantee Co.* v. *Title Guaranty Co.*, 224 U. S. 152, 155 (1912); *New York* v. *Irving Trust Co.*, 288 U. S. 329, 331 (1933); *United States* v. *Herron*, 87 U. S. 251 (1873); *In re Marine Stevedoring Corp.*, 169 Fed. (2d) 554 (C.C.A. 3, 1948); *In re Matisoff*, 36 Fed. Supp. 896 (U.S.D.C. Ga., 1941); *In re Dorb the Chemist Pharmacies*, 29 Fed. Supp. 832 (D.C. S.D. N.Y., 1939).

(e)

The Circuit Court opinion treated as without significance the fact that the Chandler Act made no changes in §17 (11 U.S.C.A. §35), which provides that tax claims are not released by a discharge in bankruptcy. While

not of paramount significance, we think this consideration of some weight. As pointed out in Judge CLARK's opinion (R. 37-38), the question of the discharge of tax claims was carefully considered. The House bill made them dischargeable but the Senate bill reverted to the old law.[1] We think it anomalous to hold that interest on tax claims need not be paid by the trustee but that they are not dischargeable by the bankruptcy. Yet that must be the effect of the ruling of the Circuit Court herein.

(f)

The Bankruptcy Act of 1898 provided in '§64a' that taxes be paid "in advance of the payment of dividends to creditors", and in §64b that debts enumerated therein to have priority be "paid in full". The Bankruptcy Act of 1898 did not list taxes in §64b among the priority claims. In 1926 (44 Stat. 666) taxes were for the first time listed in §64b among the priority claims to be "paid in full".

In the opinion of the Circuit Court in the instant case, Judge CLARK stated that the phrase "paid in full" in old §64b and present §64a, had the effect of limiting the priority of tax claims to payment of principal alone, citing *Hammer* v. *Tuffly*, 145 Fed. (2d) 447 (C.C.A. 2, 1944).

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1. The following remarks were made by Mr. Chandler as to the change in the Senate bill (Congressional Record, Vol. 83, p. 9106, June 13, 1938):

> "Dischargeability of tax claims (sec. 17): The House bill makes Federal taxes dischargeable, while the Senate amendment retains existing law in the clarifying change. The Senate felt that if Federal taxes were made dischargeable, it would open the door to evasion. The Treasury Department recommended against the House amendment."

In that case, a surplus remained after payment to creditors of the bankrupt who had filed their claims on time. The Court held that such creditors were entitled to interest on their claims to the date of payment before distribution of the surplus to a barred creditor who had not filed on time. In the course of his opinion, Judge LEARNED HAND referred to the changes in old §64b effected by the 1926 amendment to the Bankruptcy Act and suggested that they had limited the priority of tax claims to the payment of principal, relying upon certain cases in State courts holding that "payment in full" meant payment of principal only.

Prior to the 1926 amendment the law was well established that interest on tax claims in bankruptcy ran to the date of payment. See cases, *supra*, p. 6. Certainly, the inclusion of taxes among claims to be "paid in full" by the 1926 amendment could not have had the effect of delimiting interest payments on tax claims. This is particularly true in view of the fact that the 1926 amendment made no change in §57j and that section was subsequently reenacted without substantial change by the Chandler Act.

Moreover, the dictum in *Hammer* v. *Tuffy*, *supra*, seems to us to be clearly erroneous in intimating that State law could determine the manner of payment of claims in bankruptcy. Bankruptcy is a federal matter and the payment of claims therein is determined solely by Federal law. *Vanston Committee* v. *Green*, 329 U. S. 156, 163 (1946).

(3)

The views which we advocate herein are supported by most of the cases which have passed on the exact question.

Davie v. *Green*, 133 Fed. (2nd) 451 (C.C.A. 1, 1943), held that interest on a tax claim of the State of New

Hampshire in a bankruptcy proceeding should bear interest at the rate of 1% per month until the date of payment.

Carter v. *United States*, 168 Fed. (2nd) 272 (C.C.A. 2, 1948), the appeal in which is to be argued together with the instant appeal, involved tax claims of the United States and the State of New York in a bankruptcy proceeding. The District Court held that interest should run only until the date of the filing of the petition in bankruptcy. *In re Union Fabrics*, 73 Fed. Supp. 685 (D.C.S.D. N.Y., 1947). While the decision of the District Court was affirmed, the opinion of Judge AUGUSTUS N. HAND expressly states that he and Judge CHASE, constituting a majority of the Circuit Court sitting on the case, agreed with the decision in *Davie* v. *Green, supra*, but acquiesced in the decision of the District Court since it accorded with the views of the majority of the Circuit Court judges as expressed in their opinion herein. Judge CLARK, who wrote the opinion of the Circuit Court herein, sat in the *Carter* case and concurred in the result.

In re Flayton, 42 Fed. Supp. 1002 (D.C.E.D. N.Y., 1942), *In re L. Gandolfi & Co.*, 42 Fed. Supp. 706 (D.C.S.D. N. Y., 1940), *In re Summers*, 45 A.B.R. (N.S.) 123 (Ref. N.D. Ohio, 1939), and *In re Dorsey*, 46 A.B.R. (N.S.) 146 (Ref. W.D. Wash., 1940), all held that interest on tax claims in a bankruptcy proceeding runs until the date of payment.

Conclusion

The Chandler Act reenacted §57j requiring tax claims in a bankruptcy proceeding to be paid with interest, required that tax claims be filed by amending §57n, and left substantially unchanged the order of priority for tax

claim payments in the new §64a. The elimination of old §64a was an incident of the amendment to §57n requiring tax claims to be filed.

These changes do not point to any Congressional intent to change the pre-existing rule that interest on tax claims runs to the date of payment. On the contrary, by the reenactment of §57j they indicate a definite intent to leave unchanged the law as established by *United States* v. *Childs*, *supra*; *Meilink, Trustee* v. *Unemployment Reserves Commission of California*, *supra*; and other decisions (see cases, *supra*, p. 6) that interest on tax claims runs to the date of payment.

The order of the Circuit Court should be reversed, with costs, in so far as it limited the payment of interest to the date of the filing of the petition in bankruptcy, and interest on the petitioner's claim at the rate of 1% per month until the date of payment should be directed to paid.

New York, N. Y., December 3, 1948.

Respectfully submitted,

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APPENDIX

Statutes Involved

1. New York State.

In 1940 and 1941, the Legislature of the State of New York passed Enabling Acts (L. 1940, ch. 245; L. 1941, ch. 200; L. 1941, ch. 199), which authorized the City of New York to impose the sales and business tax for the periods here involved.

We have not reprinted the Enabling Acts since the case does not call for an interpretation of their language.

2. The New York City Local Laws.

The New York City sales taxes here involved were imposed pursuant to the Administrative Code of the City of New York, Chapter 41, Title N, and the business taxes were imposed pursuant to the provisions of the Administrative Code of the City of New York, Chapter 41, Titles R and RR. Each of such Titles of the Administrative Code has a provision imposing penalties and interest in case of failure to file a return or to pay taxes due as required. The provision in Title N of Chapter 41 (sales tax) reads as follows (Adm. Code, §N41-17.0, subd. a, Williams Ed., p. 2121):

> "*Penalties and interest.* a. Any person failing to file a return or to pay or pay over any tax to the treasurer within the time required by this title shall be subject to a penalty of five percentum of the amount of tax due; plus interest at the rate of one percentum of such tax for each month of delay excepting the first month after such return was required to be filed or such tax became due; but the comptroller or as provided in section N41-13.0, the

treasurer if satisfied that the delay was excusable, may remit all or any part of such penalty, but not interest at the rate of six per cent per year. Such penalties and interest shall be paid and disposed of in the same manner as other revenues from this title. Unpaid penalties and interest may be enforced in the same manner as the tax imposed by this title."

The corresponding provision of Title R and Title RR of the Administrative Code (business tax) is practically identical. (See Adm. Code, §R41-15.0, subd. a and §RR41-14.0, subd. a, Williams Ed., pp. 2165, 2176.)

3. The National Bankruptcy Acts.

The provisions of the National Bankruptcy Act relied on and referred to in the opinion of the Court below, §§17, 57j, 57n, 63a, 64a and b (11 U.S.C.A. §§35, 93j, 93n, 103a, 104a and b, respectively), as they read both before and after the Chandler Act of 1938 are set forth, *post*, pp. 24-33.

Pertinent Provisions of the National Bankruptcy Act

Before the Chandler Act

Section 17 (11 U.S.C.A. §35)

"**Debts not affected by a discharge.** A discharge in bankruptcy shall release a bankrupt from all of his provable debts, except such as (first) are due as a tax levied by the United States, the State, county, district, or municipality in which he resides; * * *."

Section 57 (11 U.S.C.A. §93)

Proof and Allowance of Claims.

* * *

(j) Debts owing to the United States, a State, a county, a district, or a municipality as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law.

* * *

(n) Claims shall not be proved against a bankrupt estate subsequent to one year after the adjudication; or if they are liquidated by litigation and the final judgment therein is rendered within thirty days before or after the expiration of such time, then within sixty days after the rendition of such judgment: Provided, That the right of infants and insane persons without guardians, without notice of the proceedings, may continue six months longer.

(*Continued on page 26*)

Pertinent Provisions of the National Bankruptcy Act

As Amended by the Chandler Act

Section 17 (11 U.S.C.A. §35)

"**Debts not affected by a discharge.** A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as (1) are due as a tax levied by the United States, or any State, county, district, or municipality; * * *."

Section 57 (11 U.S.C.A. §93)

Proof and Allowance of Claims.

* * * *

(j) Debts owing to the United States or any State or subdivision thereof as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law.

* * * *

(n) Except as otherwise provided in this title, all claims provable under this title, including all claims of the United States and of any State or subdivision thereof, shall be proved and filed in the manner provided in this section. Claims which are not filed within six months after the first date set for the first meeting of creditors shall not be allowed: *Provided, however,* That the court may, upon application before the expiration of such period and for cause shown, grant a reasonable fixed extension of time

(*Continued on page 27*)

Section 63a [11 U.S.C.A. §103(a)]

Debts provable against

(a) Debts of the bankrupt may be proved and allowed against his estate which are (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, with any interest thereon which would have been recoverable at that date or with a rebate of interest upon such as were not then payable and

(*Continued on page* 28)

for the filing of claims by the United States or any State or subdivision thereof: *Provided further*, That, except in proceedings under chapters 10, 11, 12, and 13 of this title, the right of infants and insane persons without guardians, without notice of the bankruptcy proceedings, may continue six months longer: *And provided further*, That a claim arising in favor of a person by reason of the recovery by the trustee from such person of money or property, or the avoidance by the trustee of a lien held by such person, may be filed within thirty days from the date of such recovery or avoidance, but if the recovery is by way of a proceeding in which a final judgment has been entered against such person, the claim shall not be allowed if the money is not paid or the property is not delivered to the trustee within thirty days from the date of the rendering of such final judgment, or within such further time as the court may allow. When in any case all claims which have been duly allowed have been paid in full, claims not filed within the time hereinabove prescribed may nevertheless be filed within such time as the court may fix or for cause shown extend and, if duly proved, shall be allowed against any surplus remaining in such case.

Section 63a [11 U.S.C.A. §103(a)].

Debts which may be proved

a. Debts of the bankrupt may be proved and allowed against his estate which are founded upon (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition by or against him, whether then payable or not,

(*Continued on page 29*)

did not bear interest; (2) due as costs taxable against an involuntary bankrupt who was at the time of the filing of the petition against him plaintiff in a cause of action which would pass to the trustee and which the trustee declined to prosecute after notice; (3) founded upon a claim for taxable costs incurred in good faith by a creditor before the filing of a petition in an action to recover a provable debt; (4) founded upon an open account, or upon a contract express or implied; (5) founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of the bankrupt's application for a discharge, less costs incurred and interest accrued after the filing of the petition and up to the time of the entry of such judgment; (6) founded upon an award of an industrial accident commission, or other commission, body or officer, of any State or Territory having power or jurisdiction to make awards as workmen's compensation in case of injury or death for injury prior to adjudication; (6½) the amount of any damages, as evidenced by a judgment of a court of competent jurisdiction, in any action for negligence instituted prior to adjudication of defendant in such action in bankruptcy and pending at the time of the filing of petition in bankruptcy, whether voluntary or involuntary; *Provided*, That the provisions of this clause (6½) shall apply to estates that were pending on June 7, 1934, and are in process of settlement; and (7) claims for damages respecting executory contracts including future rents whether the bankrupt be an individual or a corporation, but the claim of a landlord for injury resulting from the rejection by the trustee of an unexpired lease of real estate or for damages or indemnity under a

(*Continued on page 30*)

with any interest thereon which would have been recoverable at that date or with a rebate of interest upon such as were not then payable and did not bear interest; (2) costs taxable against a bankrupt who was at the time of the filing of the petition by or against him plaintiff in a cause of action which would pass to the trustee and which the trustee declines to prosecute after notice; (3) a claim for taxable costs incurred in good faith by a creditor before the filing of the petition in an action to recover a probable* debt; (4) an open account, or a contract express or implied; (5) provable debts reduced to judgments after the filing of the petition and before the consideration of the bankrupt's application for a discharge, less costs incurred and interest accrued after the filing of the petition and up to the time of the entry of such judgments; (6) an award of an industrial-accident commission, body, or officer of any State having jurisdiction to make awards of workmen's compensation in case of injury or death from injury, if such injury occurred prior to adjudication; (7) the right to recover damages in any action for negligence instituted prior to and pending at the time of the filing of the petition in bankruptcy; (8) contingent debts and contingent contractual liabilities; or (9) claims for anticipatory breach of contracts, executory in whole or in part, including unexpired leases of real or personal property: *Provided, however,* That the claim of a landlord for damages for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall in no event be allowed in an amount exceeding the rent reserved by the lease, without acceleration, for the year

* So in original. Should read "provable".

(*Continued on page* 31)

covenant contained in such lease shall in no event be allowed in an amount exceeding the rent reserved by the lease, without acceleration, for the year next succeeding the date of the surrender of the premises, plus an amount equal to the unpaid rent accrued up to said date: *Provided*, That the court shall scrutinize the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages allowed assignee hereunder: *Provided further*, That the provisions of this clause (7) shall apply to estates pending on June 7, 1934, in which the time for filing such claims has not expired.

Section 64 (11 U.S.C.A. §104)

Debts which have priority.

(a) The court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, State, county, district, or municipality, in the order of priority as set forth in paragraph (b) hereof: *Provided*, That no order shall be made for the payment of a tax assessed against real estate of a bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court. Upon filing the receipts of the proper public officers for such payments the trustee shall be credited with the amounts thereof, and in case any question arises as to the amount or legality of any such tax the same shall be heard and determined by the court.

(b) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment shall be

(Continued on page 32)

next succeeding the date of the surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after bankruptcy, plus an amount equal to the unpaid rent accrued, without acceleration, up to such date: *And provided further*, That in the case of an assignment of any such claim for damages, the court shall, in determining the amount thereof, examine the circumstances of the assignment and the consideration paid or to be paid therefor, and may allow the claim of the assignee in such amount, subject to the provisions of the foregoing proviso of this clause (9), as will be fair and equitable.

Section 64 (11 U.S.C.A. §104)

Debts which have priority

(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the fees for the referees' salary fund and for the referees' expense fund; the filing fees paid by creditors in involuntary cases; where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge, the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of

(*Continued on page* 33)

(1) the actual and necessary cost of preserving the estate subsequent to filing the petition; (2) the filing fees paid by creditors in involuntary cases, and, where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the expense of one or more creditors, the reasonable expense of such recovery; (3) the cost of administration, including the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases while performing the duties herein prescribed, and to the bankrupt in voluntary and involuntary cases, as the court may allow; (4) where the confirmation of composition terms has been refused or set aside upon the objection and through the efforts and at the expense of one or more creditors, in the discretion of the court, the reasonable expenses of such creditors in opposing such composition; (5) wages due to workmen, clerks, traveling or city salesmen, or servants, which have been earned within three months before the date of the commencement of the proceeding, not to exceed $600 to each claimant; (6) taxes payable under paragraph (a) hereof and (7) debts owing to any person who by the laws of the States or the United States is entitled to priority: *Provided*, That the term "person" as used in this section shall include corporations, the United States and the several States and Territories of the United States.

attorneys employed to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, as the court may allow; (2) wages, not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) where the confirmation of an arrangement or wage-earner plan or the bankrupt's discharge has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors, or, where through the efforts and at the cost and expense of one or more creditors, evidence shall have been adduced resulting in the conviction of any person of an offense under this title, the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside, or in adducing such evidence; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: *Provided*, That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further*, That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States is entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State law: *Provided, however*, That such priority for rent to a landlord shall be restricted to the rent which is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.